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Message Text

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ACTION NEA-10

INFO OCT-01 ISO-00 AGRE-00 CEA-01 CIAE-00 COME-00 DODE-00
EB-07 FRB-03 H-01 INR-07 INT-05 L-03 LAB-04 NSAE-00
NSC-05 PA-01 AID-05 CIEP-01 SS-15 STR-04 ITC-01
TRSE-00 USIA-06 PRS-01 SP-02 OMB-01 FEA-01 /085 W
----------232152Z 106533 /67
R 231320Z DEC 76
FM AMEMBASSY TEL AVIV
TO SECSTATE WASHDC 4203

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E.O. 11652: N/A
TAGS: EFIN, IS
SUBJECT: ISRAELI ECONOMY

REF: (A) TEL AVIV 8417 (B) TEL AVIV 8140

1. WE HAVE OBTAINED A COPY OF AN OFFICIAL DOCUMENT PREPARED FOR MINISTER RABINOWITZ'S USE IN SESSIONS ON THE DRAFT BUDGET WITH THE CABINET AND THE HISTADRUT LEADERSHIP AT THE END OF NOVEMBER. THE FORECASTS ARE BASED ON THE LATEST DATA AVAILABLE ON THAT DATE. HIGHLIGHTS ARE REPORTED BELOW; FULL TEXT IS BEING POUCHED TO NEA/IAI.

2. DEVELOPMENTS IN 1976
(A) PAPER LEADS OFF BY NOTING IMPROVEMENT REGISTERED IN THE BALANCE OF PAYMENTS, BUT EXPRESSES ANXIETY ABOUT "RECENT SOCIAL AND ECONOMIC UPHEAVALS WHICH COULD UNDERMINE OUR ACHIEVEMENTS". WHILE A DECLINE IN THE TRADE DEFICIT BY $150 MILLION WAS FORECAST, RECENT DATA SUGGEST REDUCTION OF $500 MILLION FROM LAST YEAR'S DEFICIT. IT IS NOTED THAT POSITIVE EXPORT TRENDS BEGAN IN 1975, WERE CONSOLIDATED IN EARLY 1976, AND
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HAVE CONTINUED IN RECENT MONTHS. TOTAL GROWTH OF EXPORTS IN 1976 WAS ESTIMATED AT 15 PER CENT IN DOLLAR TERMS. GROWTH IN EXPORTS AND RESTRAINED LEVEL OF IMPORTS ARE ATTRIBUTED TO CURTAILMENT OF LOCAL DEMAND, CREEPING CURRENCY DEVALUATION, AND RECOVERY OF WORLD MARKET DEMAND. POSITIVE TREND HAS RESULTED IN REDUCED

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PRESSURE ON FOREIGN CURRENCY RESERVES WHICH HAVE IN-
CREASED BY $100 MILLION DESPITE A $250 MILLION REDUCTION
IN SHORT TERM DEBT. THE PORTION OF SHORT TERM DEBT
IN TOTAL NATIONAL DEBT HAS THUS DECLINED FROM 12 PER
CENT LAST YEAR TO 8 PER CENT AT PRESENT.

(B) THE NATIONAL PRODUCT WILL GROW IN 1976 BY ABOUT
3 PER CENT IN REAL TERMS, AS COMPARED TO LAST YEAR'S
ONE HALF PER CENT. TOTAL PRIVATE CONSUMPTION HAS
GROWN BY 5.5 PER CENT WITH PRIVATE CONSUMPTION PER
CAPITA INCREASING BY 3 PER CENT. PAPER NOTES THAT GOI
HAD IN FACT PLANNED FOR A DROP IN PER CAPITA CONSUMPTION
OF 2 PER CENT THIS YEAR. PUBLIC CONSUMPTION DECLINED
BY 3.5 PER CENT, REFLECTING DROP OF 9 PER CENT IN
MILITARY IMPORTS AND RISE OF 2 PER CENT IN CIVILIAN
PUBLIC CONSUMPTION.

(C) ON PRICE AND LABOR FRONT, THERE HAS BEEN SOME
WEAKENING OF "DIMENSIONS OF OVER-EMPLOYMENT". TEN
THOUSAND WORKERS HAVE BEEN SHIFTED TO EXPORT IN-
DUSTRIES. ANNUAL WAGES PER EMPLOYEE HAVE RISEN BY
APPROXIMATELY 35 PER CENT WITH REAL WAGES INCREASING
BY 3 PER CENT. CONSUMER PRICES WILL GO UP BY MORE
THAN 35 PER CENT, WITH THREE QUARTERS OF PRICE RISE
STEMMING FROM DEVALUATIONS, CUTS IN SUBSIDIES, AND
INTRODUCTION OF VAT.

3. OUTLOOK FOR 1977

WHILE PROGRESS HAS BEEN MADE IN A NUMBER OF IMPORTANT
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AREAS, ISRAEL IS STILL FACED WITH DIFFICULT AND SERIOUS
PROBLEMS WHICH WILL TAKE MANY YEARS TO SOLVE. TO CON-
TINUE TO MOVE IN THE RIGHT DIRECTION, ISRAEL MUST
"MAKE SACRIFICES IN SHORT TERM, INSURE FULL EMPLOYMENT,
RESTRAIN INFLATION, IMPROVE BALANCE OF PAYMENTS, AND
CONTINUE CONSTRUCTION AND ECONOMIC DEVELOPMENT. GOVERNMENT
AND HISTADRUT SHOULD SET AN EXAMPLE".

(A) THE MAJOR PROBLEMS FACING THE ECONOMY IN 1977 WILL
CONTINUE TO BE BALANCE OF PAYMENTS DEFICIT AND INFLATION.
ALL AGREE ON NEED TO RETURN TO RAPID GROWTH AS SOON AS
POSSIBLE. HOWEVER, IT IS STILL PREMATURE TO ABANDON
SHORT TERM OBJECTIVE OF RESTRAINING EXCESSIVE ECONOMIC
ACTIVITY. DESPITE SOME WEAKENING OF THE LABOR MARKET,
THERE IS STILL A SHORTAGE OF SKILLED AND OTHER WORKERS
IN MOST INDUSTRIAL SECTORS. DEMAND MUST CONTINUE
TO BE CURBED IF INFLATION IS TO BE RESTRAINED.
THUS, 1977 IS EXPECTED TO BE ANOTHER YEAR OF RE-

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LATIVELY LOW ECONOMIC ACTIVITY, WITH GNP RISING
BY ABOUT 3 PER CENT AS IN 1976. INVESTMENT IN
INDUSTRY IS EXPECTED TO REMAIN UNCHANGED; BUILDING
SECTION WILL SEE A 15 PER CENT DROP WHILE INVESTMENT
WILL RISE IN AGRICULTURE, ELECTRIC POWER, AND
TRANSPORTATION.

(B) WHILE 1976 WILL SEE A $500 MILLION REDUCTION IN
BOP CURRENT ACCOUNT DEFICIT AND AN EQUAL DROP IN
THE TRADE DEFICIT, NO ADDITIONAL SIGNIFICANT IMPROVE-
MENT CAN BE EXPECTED IN 1977. ALTHOUGH THE CIVILIAN
DEFICIT WILL DECLINE BY $100-150 MILLION, THERE WILL
BE LARGER IMPORT PAYMENTS BECAUSE OF INCREASED IMPORTS
OF MILITARY GOODS, LARGER INTEREST PAYMENTS ON FOREIGN
DEBT, AND HIGHER PRICES OF IMPORTED GOODS. EFFORTS
TO RAISE FUNDS ABROAD MUST BE INTENSIFIED IN ORDER
TO INSURE THAT THE LEVEL OF FOREIGN CURRENCY RESERVES
FOLLOW THE TREND OF THIS YEAR'S IMPROVEMENT OF $100
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MILLION.

(C) THE CURRENT ACCOUNT DEFICIT WILL THUS REMAIN IN
NEIGHBORHOOD OF $3.5 BILLION. THE NATIONAL DEBT WILL
CONTINUE TO GROW AND BY LATE 1977 WILL REACH $10.5 BILLION,
WITH DEBT SERVICING AMOUNTING TO $1.25 BILLION.

(D) UNLESS SPECIAL STEPS ARE TAKEN TO RESTRAIN
INFLATION, CONSUMER PRICES CAN BE EXPECTED TO
INCREASE BY 30-32 PER CENT. ONLY WAY TO ACHIEVE
A SIGNIFICANT REDUCTION IN INFLATION IS WITH A
WAGE/PRICE AGREEMENT INVOLVING HISTADRUT, EMPLOYERS
AND THE GOVERNMENT. UNREASONABLE DIGRESSIONS FROM
WAGE POLICY AND LEVEL OF GOVERNMENT SPENDING COULD
CAUSE PRICE SYSTEM TO COLLAPSE. THE GOVERNMENT,
FOR ITS PART, IS RESOLVED NOT TO DEVIATE FROM THE
PLANNED BUDGETARY DEFICIT. AN APPROXIMATE WAGE
INCREASE OF 35 PER CENT IS EXPECTED IN 1977. THIS
ESTIMATE ALLOWS FOR A 13 PER CENT INCREASE IN
OCTOBER 1977.

(E) ON FUTURE GROWTH, PAPER ESTIMATES THAT THE
TURNING POINT FOR RENEWED EXPANSION WILL OCCUR IN
SECOND HALF OF 1977 OR FIRST HALF OF 1978. IN
1978, REAL GNP WILL GROW BY 5-6 PER CENT, WITH
ANNUAL RATE RISING TO 7 PER CENT IN 1979 AND TO
8 PER CENT IN 1980. GROWTH WILL BE LED BY EXPANSION
OF EXPORTS, WHICH ARE EXPECTED TO COVER 75 PER CENT
OF IMPORTS IN 1980, COMPARED TO 54 PER CENT IN 1976.

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4. COMMENT: LATEST TRADE DATA CARRIED IN PRESS
SUGGEST THAT BOP IMPROVEMENT IN 1976 WILL BE GREATER
THAN THAT INDICATED ABOVE. THIS WILL BE REPORTED
AS SOON AS IT CAN BE CONFIRMED. WITH REGARD
TO APOSSIBLE WAGE/PRICE PACKAGE, TALKS BETWEEN
GOVERNMENT AND HISTADRUT HAD REACHED VIRTUAL
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STALEMATE EVEN BEFORE THE CABINET RESIGNED. THE
ENTIRE QUESTION HAS OF COURSE NOW BEEN PUT ASIDE
FOR TIME BEING.
TOON

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Message Attributes

Automatic Decaptioning: X
Capture Date: 01 JAN 1994
Channel Indicators: n/a
Current Classification: UNCLASSIFIED
Concepts: GOVERNMENT BUDGET, ECONOMIC CONDITIONS, BALANCE OF PAYMENTS, TRADE DATA
Control Number: n/a
Copy: SINGLE
Draft Date: 23 DEC 1976
Decaption Date: 01 JAN 1960
Decaption Note:
Disposition Action: RELEASED
Disposition Approved on Date:
Disposition Authority: greeneet
Disposition Case Number: n/a
Disposition Comment: 25 YEAR REVIEW
Disposition Date: 28 MAY 2004
Disposition Event:
Disposition History: n/a
Disposition Reason:
Disposition Remarks:
Document Number: 1976TELAV08611
Document Source: CORE
Document Unique ID: 00
Drafter: n/a
Enclosure: n/a
Executive Order: N/A
Errors: N/A
Film Number: D760471-0568
From: TEL AVIV
Handling Restrictions: n/a
Image Path:
ISecure: 1
Legacy Key: link1976/newtext/t19761215/aaaaamvx.tel
Line Count: 185
Locator: TEXT ON-LINE, ON MICROFILM
Office: ACTION NEA
Original Classification: LIMITED OFFICIAL USE
Original Handling Restrictions: n/a
Original Previous Classification: n/a
Original Previous Handling Restrictions: n/a
Page Count: 4
Previous Channel Indicators: n/a
Previous Classification: LIMITED OFFICIAL USE
Previous Handling Restrictions: n/a
Reference: 77 TEL AVIV 8417, 77 TEL AVIV 8140
Review Action: RELEASED, APPROVED
Review Authority: greeneet
Review Comment: n/a
Review Content Flags:
Review Date: 14 JUN 2004
Review Event:
Review Exemptions: n/a
Review History: RELEASED <14 JUN 2004 by CunninFX>; APPROVED <07 OCT 2004 by greeneet>
Review Markings:

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US Department of State
EO Systematic Review
04 MAY 2006

Review Media Identifier:
Review Referrals: n/a
Review Release Date: n/a
Review Release Event: n/a
Review Transfer Date:
Review Withdrawn Fields: n/a
Secure: OPEN
Status: NATIVE
Subject: ISRAELI ECONOMY
TAGS: EFIN, IS
To: STATE
Type: TE
Markings: Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 04 MAY 2006

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